No. 93-1651

(3)

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

STUART K. PATRICK,

Petitioner,

—v.—

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF FOR PETITIONER

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TABLE OF CONTENTS

	PAGE
1. The importance of the case	1
2. Petitioner's right to due process	1
3. Congress' intent	3
Conclusion	6

TABLE OF AUTHORITIES

Statutes PAGE

Section 6(d)(1) of Securities Exchange Act,
15 U.S.C. § 78f(d)(1) 1

The Government's brief amply demonstrates the importance of this case, and the facts that petitioner Stuart K. Patrick was denied due process and that the kind of review envisioned by Congress was not accorded to him.

1. The importance of the case

The Government now attempts to describe this case as a run-of-the-mill Exchange determination. However, Petitioner was unanimously exonerated at the Exchange hearing and found guilty only on *appeal*. Moreover, this is admittedly a case of first impression; and it admittedly sets an important precedent. Thus, the SEC itself argued to the Court of Appeals, in seeking to get the decision below published:

> "This decision is the *first* judicial decision of which we are aware that discusses and details supervisory responsibilities of officials in brokerage firms." (emphasis added)

[A 42a; see also A 43a "the decision in this case *establishes* significant judicial authority on supervisory responsibilities in securities firms . . ." (emphasis added)].

2. Petitioner's right to due process

The SEC not only failed to provide an appropriate review (as an appellate authority), but also improperly ignored the Securities Exchange Act itself. Section 6(d)(1) of the statute specifically required that the Exchange, in bringing its disciplinary proceeding, specify the conduct which was allegedly improper and the specific provision of the Exchange rules which such conduct is deemed to violate. 15 U.S.C. § 78f(d)(1).[1]

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[1] Section 6(d)(1) reads in full text:

"In any proceeding by a national securities exchange to determine whether a member or person associated with a member should be disciplined (other than a summary proceeding pursuant to paragraph (3) of this subsection), *the exchange shall bring specific charges, notify such member or person of, and give him opportu-*

The only rule which the Exchange cited in its charge against Mr. Patrick was Exchange Rule 342(a) [A 34a], and the only conduct which was specified as a violation of that rule was Mr. Patrick's alleged failure "to reasonably discharge his duties and obligations in connection with the supervision and control of the activities of" Mr. Keller, who was allegedly an employee "under his supervision" [*id.*; see also A 33a "Patrick was the direct *supervisor* of Keller and was responsible for supervision of Keller's trading in the Account"]. Those are also the only act and rule which were the subject of the hearing and which are cited in the Exchange's hearing determination. [A 28a-31a].

Mr. Patrick was unanimously exonerated of that charge at the hearing, when every witness testified that he did not have that supervisory responsibility. There was no mention in the charge of any role or supposed responsibility of Mr. Patrick as Mr. Keller's "direct *superior* [cf. Gov. Br., p. 4], and no mention of Mr. Patrick's supposed "overall supervisory responsibility for the firm's operations" [*id.*, p. 3]. Those were new charges injected into the case at the *appeal* level, which were never the subject of the hearing and are not included in the charge.[2]

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nity to defend against, such charges, and keep a record. A determination by the exchange to impose a disciplinary sanction shall be supported by a statement setting forth—

(A) any act or practice in which such member or person associated with a member has been found to have engaged, or which such member or person has been found to have omitted;

(B) the specific provision of this chapter, the rules or regulations thereunder, or the rules of the exchange which any such act or practice, or omission to act, is deemed to violate; and

(C) the sanction imposed and the reasons therefor." (emphasis added)

[2] The word "superior" also is not found in Exchange Rule 342(a) [A 38a]. In this regard, we note that the Government's quote of that rule [Gov. Br., p. 2, n.1] omits the first part of Rule 342(a), which plainly shows that it is directed at *supervision* of *activities* of employees, not the general corporate hierarchy in the firm.

The supposed role of the SEC to review the record *de novo* surely cannot mean that the SEC can (a) re-write the charge, (b) assume what Mr. Patrick would have introduced by way of evidence if he had been so charged, and (c) simply convict him on appeal without any further hearing or even confrontation of Mr. Patrick with the new charge. In so doing, the SEC took on the role of prosecutor, judge and jury, and improperly abdicated its role as reviewing appellate authority. How is an employee of a brokerage firm ever to obtain a meaningful appellate review (as Congress plainly intended) when the reviewing authority assumes the role of accuser and trial judge? Unless this court steps in to correct this abuse of power by the SEC, the decision below will become a precedent (as the SEC itself candidly told the Court of Appeals [A 43a]) for continued serious denial of due process to persons charged in disciplinary proceedings by self-regulating organizations.

3. Congress' intent

Congress established an appellate structure for review of Exchange disciplinary proceedings in order to provide the protections of due process and justice, not to deny them. Congress's intent (as codified in the Securities Exchange Act) has plainly been undermined in this case. The SEC simply ignored the statutory requirement that the Exchange set forth the specific rule and conduct at issue in its charge against Mr. Patrick. The Hearing Panel had correctly understood that, and exonerated Mr. Patrick of the only charge against him. The SEC's change (and condoning of a change) of the charge on appeal violates Congress' directive in § 6(d)(1) of the statute.

The SEC's effort to justify its decision by reference to other rules and different conduct (e.g. Mr. Patrick's supposed duties as Mr. Keller's superior in the corporate chain of command, or as a person establishing the supervisory procedures of the firm under Exchange Rule 342(b), etc.) is the opposite of what Congress had in mind when it designated the SEC as the

reviewing appellate authority. The SEC is supposed to wear its appellate review hat in this situation, not its enforcement prosecutorial hat, as occurred here.

The Government (like the SEC) now contends that the conduct which supposedly gave rise to Mr. Patrick's guilt is his supposed "failure to establish appropriate procedures for supervision" [Gov. Br., p. 7]). There is no such language in Exchange Rule 342(a) [cf. A 38a]. The SEC's contention that such a duty is part of Rule 342(a) seeks to re-write that rule by engrafting onto it matters expressly provided in Rule 342(b). In so doing, the SEC took on a *legislative* role, at odds with its role as appellate reviewing authority. The very fact that such a duty is expressly provided in Rule 342(b) would lead any reasonable person to believe that, if one is to be charged with such a violation, the charge will be brought under and cite Rule 342(b) — as required by § 6(d)(1) of the statute. Here, Mr. Patrick was not given such notice and opportunity to defend, resulting in a serious denial of due process to him.

The Government's contention that "exchange hearing panel decisions often describe Rule 342(a) decisions in terms of the duties under Rule 342(b)" [Gov. Br., p. 7, n.4] is simply wrong. As detailed in the Courts below, Exchange hearing panel decisions do not do so, but rather show that, where violations of both Rules 342(a) and Rule 342(b) are charged, both rules are expressly cited and the specific conduct involved is expressly delineated.[3] Moreover, the governing

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[3] The Government's brief is filled with other serious factual errors and statements which are inconsistent with the record and the evidence before the Hearing Panel. For example, the Government contends that Mr. Patrick was not charged solely as Mr. Keller's designated supervisor, but rather also as his "direct corporate superior" [Gov. Br., p. 7]; a review of the Charge [A 32a-34a] shows that there was no such allegation against Mr. Patrick. Nor was there any reference to Mr. Patrick's supposedly being liable based upon "the corporate chain of command" [*id.*]. Similarly, the Government is simply wrong in contending that, even though the Charge did not advise Mr. Patrick that he might be held liable

authority in this regard is § 6(d)(1) of the Securities Exchange Act (and, of course, the Constitution), not what one exchange hearing panel may have said in one uncontested consent settlement (i.e., the one case cited by the Government for this statement).

Congress also set forth a detailed rule-making procedure in the Securities Exchange Act, whereby proposed Exchange rules are published, subject to comment and thereafter reviewed by the SEC (in a different capacity from that of the SEC as appellate reviewing authority). The language of Rule 342(a) and Rule 342(b) is clear; the two rules, on their face, address different kinds of conduct. It was not the province of the SEC, when acting as appellate reviewing authority of the disciplinary proceeding against Mr. Patrick, to decide to meld those two rules together and decree that they are interchangeable, despite their plainly different language. In doing so, the SEC once again confused its roles and failed to provide Mr. Patrick the meaningful appellate review which Congress promised him.

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for supposedly failing to establish supervisory procedures, that matter was "addressed at the hearing" [Gov. Br., p. 8, n.5]. That was not the subject of the hearing. The only evidence presented by the Exchange on that subject was a brief reference during *Respondent's* case (i.e. after the Exchange had rested) to Mr. Patrick's role and duties as President of the firm; that hardly provides "adequate notice" that, even though the Charge never mentioned the words "direct superior", Mr. Patrick might be held guilty on appeal based upon his superior corporate position. Even assuming that the SEC may have a right to make its own findings, such findings must be based upon the evidence in the record, not the whim of the SEC or the unsubstantiated contentions of the Exchange.

Conclusion

The petition for a writ of certiorari should be granted.

Dated: July 11, 1994
New York, New York

Respectfully submitted,

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